AUDITOR-GENERAL
SOUTH AFRICA

The accounting officer
Govan Mbeki Municipality
Private Bag X1017
Secunda
2302

30 November 2013

Reference: 03014REG12/13

Dear Sir

**Report of the Auditor-General on the financial statements and other legal and regulatory requirements of the municipality for the year ended 30 June 2013**

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa section 121(3) of the Municipal Finance Management Act of South Africa (MFMA)
2. We have not yet received the other information that will be included in the annual report with the audited financial statements and have thus not been able to establish whether there are any inconsistencies between this information and the audited financial statements and the reported performance against pre-determined objectives. You are requested to supply this information as soon as possible. Once this information is received it will be read and should any inconsistencies be identified these will be communicated to you and you will be requested to make the necessary corrections. Should the corrections not be made we will amend and reissue the audit report.
3. In terms of section 121(3) of the MFMA you are required to include the audit report in the municipality's annual report to be tabled.
4. Until the annual report is tabled as required by section 127(2) of the MFMA, the audit report is not a public document and should therefore be treated as confidential.
5. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
    - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.

- The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.

6. Please notify the undersigned Business Executive well in advance of the date on which the annual report containing this audit report will be tabled.
7. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed

.....
Business Executive : Mpumalanga

Enquiries: Sibongile Lubambo
Telephone: (013) 756 0800
Fax: (013) 756 0879

## REPORT OF THE AUDITOR-GENERAL TO THE MPUMALANGA PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE GOVAN MBEKI LOCAL MUNICIPALITY

## REPORT ON THE FINANCIAL STATEMENTS

### Introduction

1. I have audited the financial statements of the Govan Mbeki Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

### Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2012 (Act No. 5 of 2012) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

## Basis for qualified opinion

### Provisions

6. In terms of GRAP 19, *Provisions*, a provision must be recognised when a reliable estimate can be made of the amount of the obligation. Material differences in variables used by the current year's expert as compared to the prior period were identified in the revaluation report. No reasonable explanation could be obtained for these differences. I was unable to confirm the reason for these differences through alternative procedures. Consequently, I was unable to determine whether the provision amounting to R84 240 836 disclosed in the financial statements is fairly stated.

### Consumer debtors

7. I was unable to obtain sufficient appropriate audit evidence to support prior period adjustments to consumer debtors amounting to R57 873 916. I was unable to confirm this adjustment through alternative procedures.

8. In terms of GRAP 104, *Financial instruments*, an entity first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. The underlying data used to assess the consumer debtors for evidence of impairment was not reliable.

9. Consequently, I was unable to determine whether consumer debtors amounting to R399 868 707 disclosed in note 5 to the financial statements are fairly stated.

### Service charges

10. In terms of the GRAP *Framework for presentation and preparation of financial statements*, transactions must be recorded as they occur and not only on payment. Sale of electricity transactions that occurred during the current period were not accounted for in the current period, due to meter readings not being recorded timeously. Consequently, service charges revenue and consumer debtors are understated by R97 045 008. Furthermore, this had a consequential impact on the accumulated surpluses for the current period.

### Commitments

11. In terms of paragraph 124 of GRAP 1, *Presentation of financial statements*, the other disclosures should include unrecognised contractual commitments. Commitments disclosed in the financial statements are misstated by R102 746 494, due to management incorrectly using the budget amount instead of the contracted amount in the calculations.

### Qualified opinion

12. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Govan Mbeki Municipality as at 30 June 2013 and its financial performance, cash flows and statement of comparison of budget and actual amounts for the year then ended, in accordance with Standards of GRAP and the requirements of the MFMA and DoRA.

**Emphasis of matters**

13. I draw attention to the matters below. My opinion is not modified in respect of these matters.

**Restatement of corresponding figures**

14. As disclosed in note 49 to the financial statements, the corresponding figures for 30 June 2012 have been restated as a result of an error discovered during the year ended 30 June 2013 in the financial statements of the municipality at, and for the year ended, 30 June 2012.

**Material impairments**

15. As disclosed in note 5 to the financial statements, material impairments of R275 780 143 were incurred as a result of the provision for doubtful debt.

**REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

16. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

**Predetermined objectives**

17. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.

18. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability.

19. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development priorities. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).

20. The reliability of the information in respect of the selected development priorities or objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

21. The material findings are as follows:

**Usefulness of information**

**Presentation**

22. The National Treasury's *Guide for the preparation of the annual report* requires that explanations for variances between the planned and reported (actual) targets should be provided in all instances and should also be supported by adequate and reliable corroborating evidence. A total of 55% of the targets that had not been achieved had no explanations for the reasons for variances between planned and actual achievements reported in the annual performance report. This was due to a lack of review of the presentation of the annual performance report by management.

23. Section 46 of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) requires disclosure in the annual performance report of measures taken to improve performance where planned targets were not achieved. Measures to improve performance for 29% of the planned targets not achieved were not reflected in the annual performance report. This was due to a lack of adequate review and monitoring by management.

24. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the reliability of the measures taken to improve performance.

**Consistency**

25. Section 41(c) of the MSA requires that the integrated development plan should form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 76% of the reported targets were not consistent with the targets as per the approved integrated development plan. This was due to a lack of adequate monitoring by management.

**Measurability**

26. The FMPPI requires that performance targets should be specific in clearly identifying the nature and the required level of performance. A total of 41% of the targets were not specific in clearly identifying the nature and the required level of performance. This was because management was aware of the requirements of the FMPPI but chose not to apply the principles contained in the FMPPI.

27. The FMPPI requires that performance targets should be measurable. The required performance could not be measured for 59% of the targets. This was because management was aware of the requirements of the FMPPI but chose not to apply the principles contained in the FMPPI.

28. The FMPPI requires that the time period or deadline for delivery should be specified. A total of 53% of the targets were not time bound in specifying a time period or deadline for delivery. This was because management was aware of the requirements of the FMPPI but chose not to apply the principles contained in the FMPPI.

29. The FMPPI requires that it must be possible to validate the processes and systems that produce the indicator. A total of 24% of the indicators were not verifiable in that valid processes and systems that produced the information on actual performance did not exist. This was because management was aware of the requirements of the FMPPI but chose not to apply the principles contained in the FMPPI.

**Reliability of selected development priorities in the annual performance report**

30. The FMPPI requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The information presented with respect to the physical infrastructure and energy efficiency, services and customer care, and social and community development objectives was not reliable when compared to the source information or evidence provided. This was due to a lack of standard operating procedures for the accurate recording of actual achievements.

## Compliance with laws and regulations

31. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the general notice issued in terms of the PAA are as follows:

**Annual financial statements, performance report and annual report**

32. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected, which resulted in the financial statements receiving a qualified audit opinion.

**Expenditure management**

33. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.

**Consequence management**

34. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

**Procurement and contract management**

35. Goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, as required by SCM Regulation 17(a) and (c).

36. Sufficient appropriate audit evidence could not be obtained that bid specifications had been drafted by bid specification committees composed of one or more officials of the municipality, as required by SCM Regulation 27(3).

37. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding had been advertised for the required minimum period, as required by SCM Regulation 22(1) and 22(2).

38. Sufficient appropriate audit evidence could not be obtained that bids had been evaluated by bid evaluation committees composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality, as required by SCM Regulation 28(2).

39. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.

40. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.

41. Sufficient appropriate audit evidence could not be obtained that contracts and quotations had been awarded to only providers whose tax matters had been declared by the South African Revenue Service to be in order, as required by SCM Regulation 43.

42. Awards were made to providers who were in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM Regulation 44. Furthermore, providers failed to declare that they were in the service of the municipality, as required by SCM Regulation 13(c). Similar non-compliance had been reported in the prior year and the municipality did not take disciplinary action against the suppliers or officials involved.

43. Awards were made to providers who were in the service of other state institutions or whose directors or principal shareholders were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM Regulation 44. Similar awards had been identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process, in accordance with SCM Regulation 38(1).

44. Persons in the service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, contrary to SCM Regulation 46(2)(e), the code of conduct for councillors issued in terms of the MSA, and the code of conduct for staff members issued in terms of the MSA.

45. The municipality did not implement an SCM policy, as required by section 111 of the MFMA.

46. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations had been awarded in accordance with the legislative requirements and a procurement process that is fair, equitable, transparent and competitive, as not all SCM processes had been followed.

**Revenue management**

47. An adequate management, accounting and information system was not in place to account for revenue and receipts of revenue, as required by section 64(2)(e) of the MFMA.

**Strategic planning and performance**

48. The municipality did not have and maintain effective, efficient and transparent systems of financial and risk management and internal controls, as required by section 62(1)(c)(i) of the MFMA.

49. The municipality did not establish a performance management system, as required by section 38(a) of the MSA.

50. The municipality did not conduct its affairs in a manner consistent with its integrated development plan, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and Municipal Planning and Performance Management Regulation 6.

51. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the MSA.

52. The municipality did not set key performance indicators, including input indicators, output indicators and outcome indicators, in respect of each of the development priorities and objectives set out in the integrated development plan, as required by section 41(1)(a) of the MSA and Municipal Planning and Performance Management Regulations 1 and 9(1)(a).

53. The annual performance report for the year under review did not include the performance of the municipality and each external service provider, a comparison of the performance with set targets, and measures taken to improve performance, as required by section 46(1) of the MSA.

## Internal control

54. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

### Leadership

55. Management did not perform adequate reviews of the financial and annual performance report, as material findings were not identified by management controls.

56. The municipality did not hold performance management and reporting staff accountable for shortcomings identified during the internal and external audit processes.

57. Prolonged suspension periods did not appear to be reasonable in the circumstances.

### Financial and performance management

58. Management did not always prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information.

59. Management did not always implement controls over daily and monthly processing and reconciling of transactions.

Auditor-General

Nelspruit

30 November 2013

AUDITOR-GENERAL
SOUTH AFRICA

*Auditing to build public confidence*